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Tax Appeal Tribunal Nullifies VAT on Imported Services.

Re: Gazprom Oil and Gas Ltd. V. FIRS:

Introduction

The Tax Appeal Tribunal (TAT) sitting in Abuja has ruled that services rendered by non-resident companies to Nigerian companies are not liable to VAT, except the services were performed in Nigeria or VAT is included in their invoices to their Nigerian clients.

The judgment was made on a matter brought before the TAT by Gazprom Oil and Gas Limited, against the Federal Inland Revenue Service (FIRS), over a VAT assessment on payments made to some of its foreign based consultants for consulting and research services.

The Case in Brief

Gazprom Oil and Gas Limited (the Appellant) had engaged the services of some non-resident consultants, whose invoices it had settled without charge or payment of VAT to FIRS. FIRS had subsequently carried out an audit of the company and served it with notices of VAT assessment on the transactions with foreign consultants.

The appellant argued that the transactions are not liable to VAT, as the consultants did not carry on business in Nigeria, as envisaged in Section 10 (1) of the VAT Act. The consultants were therefore under no obligation to include VAT on their invoices, to be deducted and paid to FIRS as enshrined in Section 10 (2) of the VAT Act.
The appellant believed that Section 10 of the VAT Act only makes it mandatory for non-resident companies to register for VAT and include VAT in invoices, if such non-resident companies were carrying on business in Nigeria.

The appellant also argued that FIRS demand for companies to recognise and charge VAT on transactions with non-resident companies, was in following with the 'destination principle' of VAT, as practiced in some countries, but which is not mentioned in the Nigerian VAT Act.

In its argument, FIRS presented that the destination principle applies to the transaction. That is, the place of consumption of the goods or services is where the VAT is payable. The transaction is therefore liable to VAT in Nigeria since the receiver of the service is in Nigeria.

They also argued that a physical presence is not required for a company to successfully carry on business in Nigeria and that a VAT invoice is not a precondition for the payment of VAT on an imported service

Review of Section 10 of the VAT Act

A reading of the judgment confirms that the major arguments centred on the provisions of Section 10, subsection 1 and subsection 2 of the VAT Act, which provide as follows:

"10. Registration by non-resident companies.

(1) For the purpose of this Act, a non-resident company that carries on business in Nigeria shall register for the tax with the Board, using the address of the person with whom it has a subsisting contract, as its address for purposes of correspondence relating to the tax.

(2) A non-resident company shall include the tax in its invoice and the person to whom the goods or services are supplied in Nigeria shall remit the tax in the currency of the transaction."

Before now, the practice with FIRS and of the industry at large, is to apply the reverse charge principle on all transactions with non-resident entities, when a Nigerian company is paying for services. The reverse charge principle simply requires the payer for service to account for VAT to FIRS, unlike the usual practice where the provider of service collects and account for VAT.

The above practice appears to be in line with the same Section 10, if subsection 2 is read as standing alone from subsection 1, by the fact that subsection 2 does not include the mention of 'carrying on business' in Nigeria. The judgment of the TAT however seems to prefer that the two are read as if subsection 2 is a subset of subsection 1, making it unnecessary for the mention of the need for the non-resident company to be carrying on business in Nigeria.

A Lacuna?

It is obvious that the TAT judgment has been given to the appellant mainly because of the technical deficiency of the VAT Act in its attempt to bring imported services under the Act. It is therefore instructive to note that unless this judgment is successfully challenged in a higher court, VAT on all imports (goods and services) would have been deemed illegal and FIRS estopped from demanding same.

If this happens, then Nigeria would probably have become the only country that imposes VAT on local supplies but exempts imports from the same tax. How sustainable this will be remains to be seen.

We expect FIRS to be swift in appealing this judgment and obtaining a stay of its execution, as anything to the contrary will have far-reaching implications not just for FIRS but for the entire economy, especially under the current situation when oil revenues to the federation account have nosedived.

Conclusion

The judgment is a ground breaking one because it changes the dynamics of VAT on international transactions as currently practiced in Nigeria, which is mainly based on the destination principle using the reverse-charge approach.

The judgment has however raised more questions than it sought to answer, such as: how will exported services be treated for VAT? Will the Origin principle be applied in deciding what constitute exported services? What was the intention of the lawmakers in drafting Section 10 of the VAT Act? Was the intention to exempt imported goods and services from VAT, while maintaining the tax on local supplies? Will taxpayers be justified to demand for a refund of VAT paid over the years on imported services?

In our view the best way of answering the many questions thrown up by the shallowness of the VAT Act, as it is today, is to carry out a total re-enactment of the Act in line with global best practice. This action has been delayed for too long already.

We therefore advise companies to exercise restraint in implementing this judgment, pending the outcome of subsequent appeals by FIRS, which we are confident will not be long in coming.

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